

STATE OF CALIFORNIA
DEPARTMENT OF INSURANCE
45 Fremont Street, 21st Floor
San Francisco, California 94105

INITIAL STATEMENT OF REASONS

Date: March 15, 2002

RH399

PROPOSED AMENDMENTS TO THE FAIR CLAIMS SETTLEMENT
PRACTICES REGULATIONS PURSUANT TO INSURANCE CODE
SECTION 790.10

INTRODUCTION:

Pursuant to California Insurance Code Section 790.10, California Insurance Commissioner Harry Low ("Commissioner") proposes amendments to California Code of Regulations, Title 10, Chapter 5, Subchapter 7.5, entitled "Fair Claims Settlement Practices Regulations". The original regulations, effective January 13, 1993, were promulgated to provide definitive standards of conduct to insurers and other licensees for compliance with the Insurance Code's unfair claims settlement practices statute, Section 790.03(h). These regulations were amended effective May of 1997.

After working with the amended regulations for close to four years, it has become apparent that additional modifications need to be made as follows:

- 1) Reorganize the subsections so that they are easier to understand and use.
- 2) Add or delete language for reasons of grammar or clarity.
- 3) Eliminate unnecessary portions of the regulations in cases where existing laws adequately cover the subject area.
- 4) Add subsections where necessary in order to set forth reasonable standards of conduct in the handling of claims.

The Commissioner believes that the following amendments to the regulations are necessary to ensure that the claims handling standards prescribed by the legislature in California Insurance Code Section 790.03(h) are adequately implemented.

SPECIFIC PURPOSE AND REASONABLE NECESSITY OF REGULATION:

The specific purpose of each adoption, amendment, or repeal and the rationale for the Commissioner's determination that each

adoption, amendment or repeal is reasonably necessary to carry out the purpose for which it is proposed is set forth below.

SECTION 2695.1. Preamble.

Section 2695.1(a) **Amend**

Existing subsection 2695.1 refers to Insurance Code Section 790.03(h) and the promulgation of the subject regulations.

This subsection has been amended to replace the word "which" with "that". This amendment was made for grammatical reasons.

Section 2695.1(b) **Amend**

Existing subsection 2695.1(b) sets forth the authority under which these regulations are promulgated and the intended scope of these regulations by providing that other acts not specifically delineated in these regulations may also violate California Insurance Code Section 790.03(h).

This subsection has been amended to delete the words "pursuant to the provisions of California Insurance Code Section" and to add the word "or". This amendment was made to clarify the regulations. Amendments were also made to clarify that these regulations apply to all claims subject to Section 790 et seq. of the California Insurance Code (the "Unfair Practices Act").

Section 2695.1(c) **Repeal**

Existing subsection 2695.1(c) specifies that these regulations do not apply to the handling or settling of claims brought under surety bonds.

The proposed change to this subsection is to repeal it entirely. Even though a unique tripartite relationship exists between the surety insurer, beneficiary of the surety bond and the principal, the claims handling process is no more cumbersome with respect to the processing of these claims than in the more traditional first or third party claims setting. Therefore, certain minimum standards set forth in the regulations should and do apply to claims brought under surety bonds. For example, section 2695.7 of the regulations does not impede the surety's ability to conduct its business efficiently and fairly and in accordance with California Insurance Code Section 790.03(h).

Section 2695.1(d) **Amend** (Re-lettered only)

Existing subsection 2695.1(d) is re-lettered and is now designated

subsection 2695.1(c).

Section 2695.1(e) **Repeal**

Existing subsection 2695.1(e) specifies that these regulations shall not apply to liability insurance for the professional malpractice of health care providers (medical malpractice insurance).

The proposed change to this subsection is to repeal it entirely as medical malpractice insurance is already excluded under these regulations under subsection 2695.1(b)(2).

Section 2695.1(d) **Adopt**

The language in this newly adopted subsection clarifies that these regulations apply, as a matter of law, to claims brought under home protection contracts written by home protection companies. Insurance Code Section 12743(d)(7) specifically provides that Insurance Code Section 790 et seq. (The Unfair Practices Act) is applicable to home protection contracts and home protection companies. As both home protection companies and contracts are subject to the Unfair Practices Act, the Insurance Commissioner has clear authority under Insurance Code Section 790.10 to adopt regulations applicable to them.

Section 2695.1(f) **Amend** (Re-lettered only)

Existing subsection 2695.1(f) has been re-lettered and is now designated as subsection 2695.1(e).

Section 2695.1(f) **Adopt**

The language in this newly adopted subsection sets forth minimum standards for claims handling by insurers. This language clarifies that policy language shall not circumvent and/or fall short of those minimum standards.

NOTE-Section 2695.1 **Amend**

Section 12743 of the California Insurance Code is added as reference. This section specifies that Insurance Code Section 790 et seq. applies to home protection contracts and companies.

Section 2695.2. Definitions.

Section 2695.2(a)(2) **Amend**

The proposed minor grammatical changes to this subsection were made for clarity purposes.

Section 2695.2(g) **Amend**

Existing law defines "gross settlement amount", in pertinent part, as "the amount of the draft tendered".

This subsection has been amended by striking the words "of the draft" since insurance claims payments may be made with a check or other financial instruments as well as with a draft.

Section 2695.2(i) **Amend**

Existing law enumerates those individuals or entities that fall under the definition of "insurer".

This subsection has been amended to include the California Earthquake Authority and home protection companies within these regulations' definition of "insurer". These entities should be included within the definition as they both transact insurance and are subject to Insurance Code Section 790.03(h) and the regulations promulgated pursuant to Insurance Code Section 790.10. Language is also added to clarify that these regulations apply to all entities subject to Insurance Code Section 790.03(h) except those specified in this subsection.

Section 2695.2(j) **Amend**

Existing law defines "insurance policy".

This subsection has been amended to include within these regulations' definition of "insurance policy" home protection contracts and certificates or contracts of insurance issued by the California Earthquake Authority. The word "Plan" is also added as it had been unintentionally omitted from the name "California Automobile Assigned Risk Plan". Additionally, the word "Plan" is substituted for "plan" after "California Fair" as the "p" should be capitalized. The word "California" is also added before the words "Insurance Code" for clarification purposes. So as to make this subsection consistent with other changes made in the regulations relating to surety insurers, language has been deleted that excluded surety bonds from within the term "insurance policy".

Section 2695.2(k) **Amend**

Existing law defines "investigation".

Minor changes have been made to this subsection for clarification

purposes.

Section 2695.2(1) **Amend**

Existing law defines "knowingly committed."

This subsection has been amended to define "knowingly" so as to be consistent with amendments to subsection 2695.12(a).

Section 2695.2(s) **Amend**

Existing law defines "proof of claim."

This subsection is amended to include evidence or documentation received from sources other than the claimant that reasonably supports the claim. The insurer may have access to information that supports the claim but is not in the claimant's possession. This information should also be considered by the insurer and should not be discounted just because it does not come from the claimant.

NOTE-Section 2695.2 **Amend**

Section 995.130 of the California Code of Civil Procedure is added as authority as it provides a definition of "beneficiary" under a surety bond.

Section 2695.3. File and Record Documentation

NOTE-Section 2695.3 **Amend**

Section 790.04 of the California Insurance Code is added as authority as the Department's examination of insurance claim files is authorized under this section.

Section 2695.4. Representation of Policy Provisions and Benefits.

Section 2695.4(a) **Repeal**

This language is repealed because its substance was merged into amended subsection 2695.4(a), discussed below.

Section 2695.4(a) **Amend** (Re-lettered)

The current subsection is renumbered as subsection 2695.4(a). Existing law currently requires certain standards for claims under a surety bond. As the same standards are applicable to all claims

(not just surety), the broader words "any insurance policy" are added. The words "misrepresent" and "fail to disclose" are also added as the word "conceal" does not adequately address the insurer's obligation of disclosure to its insured or to the beneficiary of a surety bond. Additional language changes are made for clarification purposes.

Section 2695.4(a)(1) **Adopt**

The language currently contained in the second sentence of subsection 2695.4(a) is stricken and is now found in subsection 2695.4(a)(1). The change was made so that the regulations are easier to understand and use.

Section 2695.4(b) (Re-lettered only)

Existing subsection 2695.4(c) has been re-lettered and is now designated as subsection 2695.4(b).

Section 2695.4(c) **Amend** (Re-lettered only)

Existing subsection 2695.4(d) has been re-lettered and is now designated as subsection 2695.4(c).

Section 2695.4(d) **Amend** (Re-lettered)

Existing subsection 2695.4(e) has been re-lettered and is now designated as subsection 2695.4(d). The word "the" was added to subsection 2695.4(d)(2).

Section 2695.4(e) **Amend** (Re-lettered only)

Existing subsection 2695.4(f) has been re-lettered and is now designated as subsection 2695.4(e).

Section 2695.4(f) **Amend** (Re-lettered only)

Existing subsection 2695.4(g) has been re-lettered and is now designated as subsection 2695.4(f).

Section 2695.5. Duties upon Receipt of Communications.

Section 2695.5(d) **Amend**

Existing law specifies that, upon receiving notice of claim, licensees and claims agents must immediately transmit notice of claim to the insurer. The remainder of the subsection has been deleted because the language is ambiguous. Regardless of the insurer's good or bad instructions as to the proper handling of a

notice of claim, licensees and claims agents are charged, under current subsection 2695.1(f)/proposed subsection 2695.1(d), with knowledge of the regulations including the duty to immediately transmit notice of claim.

Section 2695.5(e) **Amend**

Existing law makes reference to subsection 2695.5(e)(4), which subsection inadvertently makes the requirements of subsection 2695.5(e) inapplicable to life and disability insurance. As the proposed amendment deletes subsection 2695.5(e)(4) from the regulations (see explanation below), the reference to subsection 2695.5(e)(4) is also deleted.

Section 2695.5(e)(4) **Repeal**

Existing law mistakenly makes the requirements of subsection 2695.5(e) inapplicable to life and disability insurance. The proposed deletion of subsection 2695.5(e)(4) corrects this mistake.

NOTE-Section 2695.5 **Amend**

Insurance Code Section 790.04 is added as authority as the Department is authorized under this statute to examine and investigate the claims handling activities of every person engaged in the business of insurance in this state.

Section 2695.6. Training and Certification.

Section 2695.6(b)(3) **Amend**

The reference to "independent adjusters" is vague under the existing law. This subsection is amended so as to refer to "insurance adjusters" as defined under Insurance Code Section 14021. The words "on an annual basis" are deleted as they are redundant (the subsection already includes the word "annually.")

Section 2695.7. Standards for Prompt, Fair and Equitable Settlements.

Section 2695.7(a) **Amend**

This subsection is amended to specify that no insurer may discriminate on the basis of age in addition to other already enumerated bases.

Section 2695.7(b) **Amend**

This subsection is amended to specify that the amounts accepted or denied by an insurer shall be clearly documented in the claim file. By requiring this documentation, Department examiners, in reviewing insurer claim files, will be able to determine what amount of the claim the insurer should have paid under Section 2695.7(h).

Section 2695.7(b)(1) **Amend**

The current subsection sets forth specific standards for prompt, fair and equitable settlements. This subsection is amended to clarify that these standards apply to surety bond claims.

Section 2695.7(b)(3) **Amend**

Existing law specifies that total claim denials trigger the requirement that insurers notify claimants in writing that the claim may be reviewed by this Department. This subsection is amended to clarify that partial claim denials also trigger the notification requirement.

Section 2695.7(b)(4) **Amend**

Existing law inadvertently exempts life insurance claims from the time frame requirements of subsection 2695.7(b) due to an incorrect interpretation of Insurance Code Section 10172.5 as having provided its own time frame. Language is deleted from this subsection to correct the error. The amended language also clarifies that the time frame requirements in subsection 2695.7(b) do not apply to disability income claims. Language is also added to clarify that only the time frame provision in subsection 2695.7(b) is inapplicable to the lines of insurance referred to in subsection 2695.7(b)(4). The word "California" is added before the words "Insurance Code" for clarification purposes.

Section 2695.7(b)(5) **Adopt**

The language of this newly adopted subsection was moved from Section 2695.8(k) which subsection only pertained to auto claims to the 2695.7 section that applies to all types of claims. Depreciation, betterment and salvage calculations are not limited to the handling of auto claims but are also prevalent in the adjustment of other property losses (such as homeowners' losses.) The minimum standards set forth for automobile claims should apply to all property losses.

New language was also adopted, "the cost of labor is not subject to depreciation." This language is warranted because, while property itself may depreciate, labor to replace that property is a cost that should be borne by the insurer regardless of whether the property replaced is new or used.

Section 2695.7(c)(1) **Amend**

Minor grammar and punctuation changes are made to this subsection.

Section 2695.7(d) **Amend**

Language has been added so as to be consistent with current case law (which is cited below as additional authority for Section 2695.7.) The final line of the current subsection is deleted, as it is unnecessary. The law of constructive notice already exists regardless of whether it is referred to in these regulations.

Section 2695.7(e) **Amend**

This subsection was amended to clarify that these standards apply to surety bond claims.

Section 2695.7(f) **Amend**

In the proposed amendment, the word "timely" is deleted for reasons of clarity. The last sentence of this subsection is deleted because, regardless of whether a consumer is represented by counsel, these regulations are intended to promote fairness. The insurer and claimant (whether represented or not) may have different interpretations of time limits and tolling periods. The parties should be encouraged to communicate rather than remain unaware of these potentially different views so as to avoid unnecessary litigation.

Section 2695.7(g)(2) **Amend**

The proposed language is added for reasons of clarity.

Section 2695.7(g)(7) **Amend**

This subsection is amended so that the Commissioner can take into account initial as well as final offers in determining whether a settlement offer made by an insurer is unreasonably low.

Section 2695.7(h) **Amend**

The words "in whole or in part" are added to clarify the regulation's intention of requiring payment to claimants of any amounts that have been accepted by the insurer. The words "or otherwise take action to perform its claim obligation" are added to clarify that an insurer's obligation, in addition to paying a claim, may include the taking of certain action such as defending

a lawsuit. The following amendment is also proposed: ~~The of the amount of the claim to be tendered is the amount that has been accepted which has been determined and is not disputed by the insurer as specified in subsection 2695.7(b).~~ The proposed amendment makes it clear, pursuant to subsection 2695.7(b), an insurer is required to pay the amount of the claim that it has accepted. Additional amendments were made for reasons of clarity.

Section 2695.7(h)(1) **Amend**

The reference to life insurance is deleted from this subsection (and a reference to time frame is added) in order to make it consistent with subsection 2695.7(b)(4). In addition, the exemption of fire insurance from Section 2695.7(h) is deleted because Insurance Code Section 2057 only applies where there is a written agreement or settlement between the insurer and claimant as to the amount of loss and liability of the insurer. In instances where there has been no final agreement or settlement, the insurer is still required to pay undisputed portions of the claim and should make these payments within the time frame specified in 2695.7(h). The time frames in Insurance Code Section 2057 and subsection 2695.7(h) are not in conflict and, as indicated above, there is good reason to make subsection 2695.7(h) applicable to fire claims. The word "California" is also added before the words "Insurance Code" for clarification purposes.

Section 2695.7(k) **Amend**

This subsection is amended to reflect the repeal of Insurance Code Section 1871.1(a) and the enactment of Penal Code Section 550 in place of Section 1871.1(a). The word "California" is also added before the words "Insurance Code" for clarification purposes.

Section 2695.7(n) **Amend**

This subsection was amended to eliminate language that was so narrow that it excluded certain types of insurance to which the subsection was intended to apply (such as disability income insurance where the issue is whether the medical exam is necessary to determine if the claimant is disabled.)

Section 2695.7(p) **Adopt**

The language currently contained in subsection 2695.8(i) is re-lettered as subsection 2695.7(p) to clarify that the subrogation procedures specified in these regulations should apply to other types of insurance as well as to auto insurance.

Section 2695.7(q) **Adopt**

The language currently contained in subsection 2695.8(j) is re-lettered as subsection 2695.7(q) to clarify that the subrogation procedures specified in these regulations should apply to other types of insurance as well as to auto insurance.

Section 2695.7(r) **Adopt**

This newly adopted subsection specifies that no insurer shall attempt to subrogate without having conducted a thorough, fair and objective investigation. This language is added for purposes of clarity and so as to be consistent with subsection 2695.7(d).

Section 2695.7(s) **Adopt**

This newly adopted subsection specifies that insurers are responsible for the accuracy of the data they use in evaluating and settling claims. This language was added because consumer complaints and Department examinations of insurers have revealed a lack of documented support for the claims settlement amounts offered or paid to claimants.

Section 2695.7(t) **Adopt**

This newly adopted subsection was adopted to incorporate Business and Professions Code Section 6149.5 into the regulations. Section 6149.5 requires an insurer to notify a claimant who is represented by an attorney that his or her claim has been settled and the amount of the settlement.

NOTE: Section 2695.7 **Amend**

Additional case law is cited as authority consistent with changes made to subsection 2695.7(d). Insurance Code Sections 10350.10 was added as authority in connection with insurer requests for medical examinations. Insurance Code Section 10111.2 was added as authority in connection with disability income insurance as noted in subsection 2695.7(b)(4). California Penal Code Section 550 was added as reference (regarding the amendment to subsection 2695.7(k)), reflecting the repeal of IC Section 1871.1(a) and its replacement by Penal Code Section 550). Business and Professions Code Section 6149.5 was also added as reference.

Section 2695.8. Additional Standards Applicable to Automobile Insurance.

Section 2695.8(a)(1) **Amend**

Minor changes are made to this subsection for grammatical reasons.

Section 2695.8(a)(2) **Repeal**

The language of this subsection is struck but is replaced with substantially similar language in proposed subsection 2695.8(b)(2)(see below).

Section 2695.8(b) **Amend**

Existing law refers to the adjusting and settlement of first party automobile insurance losses on the basis of actual cash value or replacement with a comparable vehicle. As first party automobile insurance includes more than actual cash value and replacement type policies (ex: stated value policies), this subsection is amended to place all first party automobile insurance policies within the scope of these regulations. The term "first party" was also struck so as to require total loss valuation standards for third party automobile claims. The valuation of automobiles should be consistent whether it involves a first or third party claimant. The word "methods" is also replaced with the more appropriate word, "standards".

Section 2695.8(b)(1) **Amend**

This subsection was revised for reasons of clarity. The main change was the removal of the word "purchase" to avoid the erroneous perception that the total loss vehicle has to be replaced in order for the taxes and fees to be included in the cash settlement. Specific language is also added to reaffirm the premise that a loss vehicle need not actually be replaced in order for taxes and fees on the comparable vehicle to be paid. New language "license fees and other annual fees computed based upon the remaining term of the loss vehicle's current registration" was added to reflect the current standard in reimbursing unused DMV fees. The claimant, after turning over title to the insurer is unable to collect the unused fees from the Department of Motor Vehicles ("DMV"). Since the insurer, as the new owner of the loss vehicle, may seek reimbursement from DMV, the insurer should reasonably pay the claimant these fees. Further, under this subsection, as currently written, insurers were required to pay claimant a full year's annual fee instead of just the unused portion of the annual fee. This would result in claimant receiving more than the amount required to indemnify claimant. In order that claimants are made whole but are not over-compensated, annual fees, such as license fees, are to be reimbursed to claimant based upon the remaining term of the loss

vehicle's current registration. Additionally, the last line of subsection 2695.8(b)(1) has been moved, with slight modification, to subsection 2695.8(b)(3).

Section 2695.8(b)(1)(A) **Adopt**

This newly adopted subsection reaffirms this Department's position that the claimant is entitled to collect taxes and fees in the settlement of the claim even if the claimant chooses to retain the loss vehicle. The subsection also provides a reasonable standard for determining the salvage value of the loss vehicle. Insurers must also disclose in writing to a claimant who retains the salvage that notice of the salvage retention must be reported to the DMV (which notification will result in the vehicle being identified as a "salvage vehicle" thus reducing its future resale and insured value).

Section 2695.8(b)(2) **Adopt**

Language contained in subsection 2695.8(a)(2), which defined "comparable vehicle", has been moved and expanded upon in this newly adopted subsection. It was moved because the language is most applicable to the portion of the regulations that deals with total automobile losses, subsection 2695.8(b). The additional language adopted includes:

"Newer model year automobiles may not be used as comparable automobiles unless there are not sufficient comparable automobiles of the same model year to make a determination as set forth in Section 2695.8(b)(3), below." When newer model year vehicles are used in a valuation, the insurer will apply a deduction to the value to adjust for this model year difference. However, in many cases, the dollar amount of these deductions cannot be supported. In many valuations reviewed by this Department, newer model year vehicles were used as comparable vehicles when there were sufficient vehicles of the same model year to determine the cost of a comparable vehicle. This language was added to ensure that same model year vehicles are used as comparable automobiles in cases where a sufficient number exists to determine a value. This will reduce the frequency of using an unsupported deduction from value when new model year vehicles are used.

"The cost of a comparable automobile is the asking price or actual sale price of that automobile." In the majority of total loss valuations reviewed by the Department, a hypothetical "take price" was used to set the value of the comparable automobile. Extensive investigation has been undertaken by the Department on this subject and it has been concluded that these "take prices" do not

accurately reflect the actual price these comparable automobiles sold for in the marketplace. In some cases, the take prices were thousands of dollars below these vehicles' actual sale prices. The Department position is that in most cases only the prices of vehicles actually sold should be used to value a loss vehicle. If an insurer chooses to use a yet unsold vehicle as a comparable automobile, it must use the ask price of that vehicle.

"Any adjustments from the cost of a comparable automobile must be discernible, measurable, itemized, and specified as well as appropriate in dollar amount and so documented in the claim file. Deductions taken from the cost of a comparable automobile that cannot be supported shall not be used. The actual cost of a comparable automobile shall not include any deduction for the condition of a loss vehicle unless the documented condition of the loss vehicle is below average for that particular year, make and model of vehicle." After extensive investigation on this subject, the Department has concluded that many of the adjustments from the cost of the comparable automobile applied by insurers cannot be supported. This language was adopted to clarify that insurers have the onus of ensuring that deductions used in a valuation are supported. Also, this language addresses the most prevalent deduction applied to vehicle values, that of condition. It has been concluded that the majority of these deductions for condition have not been supported. In these cases, the insurer makes an assumption that the loss vehicle is in worse condition when compared to the comparable vehicles used in the valuation. However, in most instances, these comparable automobiles have not been inspected for condition. Therefore, applying a deduction based upon this unsupported assumption should be prohibited. For this reason, the adopted language only permits a deduction for condition when the loss vehicle is in below average condition.

"This subsection shall not preclude deduction for prior and/or unrelated damage to the loss vehicle." This language was adopted to recognize the difference between a deduction for condition of the loss vehicle (as discussed above) and situations where the loss vehicle has prior and/or unrelated damage. Deductions for this damage should be reasonably permitted as long as the insurer fairly values this prior damage to the loss vehicle.

"The comparable automobiles used to calculate the cost shall be identified by the vehicle identification number (VIN), the stock or order number of the vehicle from a licensed dealer, or the license plate number of that comparable vehicle. The identification shall also include the telephone number (including area code) or street address of the seller of the comparable automobile." In many total loss claims investigated by the Department, the comparable

automobiles used to set the value of the loss vehicle cannot be properly identified. It is important that the comparable vehicles used to value a loss vehicle be identified in order for the claimant to have the opportunity to contact these vehicle owners to verify whether these comparable vehicles are in fact similar to the loss vehicle.

Section 2695.8(b)(3) **Adopt**

The last sentence of subsection 2695.8(b)(1) has been moved to this subsection. Language is also taken from current subsection 2695.8(b)(1)(C) which specifies that insurers must take reasonable steps to verify the accuracy of the value determined for the comparable vehicle. These changes were made for reasons of clarity.

Section 2695.8(b)(3)(A) **Amend** (Re-lettered only)

Current subsection 2695.8(b)(1)(A) is now designated subsection 2695.8(b)(3)(A) because language was added as referred to above.

Section 2695.8(b)(3)(B) **Amend** (Re-lettered)

Current subsection 2695.8(b)(1)(B) is now designated subsection 2695.8(b)(3)(B) because language was added as referred to above. Additionally, the words "were not available" and "in the last 90 days" were added to be consistent with the language in proposed subsection 2695.8(b)(3)(A).

Section 2695.8(b)(3)(C) **Adopt**

The language in this newly adopted subsection reflects the fact that, in almost every automobile total loss claim adjusted in California, insurers utilize one or more computerized total loss valuation services.

Section 2695.8(b)(3)(D) **Amend** (Re-lettered)

The amendment of this subsection provides for the use of alternative methods if the methods in (A), (B) or (C) above are unable to be performed. The word "value" was replaced with "cost" or "cost of a comparable automobile" to provide consistency with other subsections of these regulations. The words "including deduction for salvage" are deleted as this issue is addressed in revised subsection 2695.8(b)(1)(A). The last line of this subsection is deleted as it has been moved in substantially the same form to subsection 2695.8(b)(3) above.

Finally, current subsection 2695.8(b)(1)(C) is now designated subsection 2695.8(b)(3)(D) because language was added as referred to above.

Section 2695.8(b)(4) **Amend** (Re-lettered)

Current subsection 2695.8(b)(2) is now designated subsection 2695.8(b)(4) because language was added as referred to above. In addition, the words "over all" were changed to "overall" for grammatical reasons. Since subsection 2695.8 as proposed sets forth standards for both first and third party claims, and this subsection only concerns first party claims, the reference to "first party" has been added.

Section 2695.8(c) **Amend**

Since subsection 2695.8 as proposed sets forth standards for both first and third party claims, and this subsection only concerns first party claims, the reference to "first party" has been added. The words "shall apply" were deleted to correct a grammatical error. The word "draft", the meaning of which is too narrow, is changed to "payment". The procedure set forth in this subsection is a two-step procedure. The insurer must first notify the insured that if he or she cannot purchase a comparable vehicle for the gross settlement amount, he or she may contact the insurer. Second, if contacted by the insured, the insurer shall reopen the claim and follow additional procedures as set forth in subsections 2695.8(c)(1) through (3). The changes made to this subsection are intended to clarify this two-step process.

Section 2695.8(c)(1) **Amend**

The reference to 2695.8(b)(2) is changed to 2695.8(b)(4) to reflect the change in that particular subsection number.

Section 2695.8(e) **Amend**

This subsection was revised and split into subsections 2695.8 (e), (f) and (g) to clarify the distinction between an insurer "requiring" that an automobile be repaired in a particular shop (which is not permitted) and an insurer merely suggesting or recommending that an automobile be repaired in a particular repair shop (which is permitted under certain circumstances as set forth below).

Section 2695.8(f) **Amend** (Re-lettered)

Current subsection 2695.8(e)(1) is now designated subsection

2695.8(f). This subsection is revised to delete the word "direct" as this term is unnecessary in light of the terms "suggest" and "recommend" contained in this subsection. Additionally, the term "direct" may imply "require" which is prohibited under subsection 2695.8(e). Additional language was deleted as redundant.

Section 2695.8(g) **Adopt**

The language in this newly adopted subsection is added to recognize the existence of insurance contracts that specifically suggest or recommend that an automobile be repaired in a particular shop. The unique nature of these contracts requires particular disclosure standards as set forth below in subsections 2695.8(g)(1) and (2).

Section 2695.8(g)(1) **Adopt**

The language in this newly adopted subsection requires that an insurer disclose this unique contractual provision at the time a consumer applies for the insurance coverage so that the consumer has adequate notice of these policy terms.

Section 2695.8(g)(2) **Adopt**

The language in this newly adopted subsection specifies that an insurer that, by contract, suggests or recommends that an automobile be repaired in a particular shop may not receive a windfall when an insured chooses to have the insured vehicle repaired at the shop of his or her choice. Basing repair costs on discounted repair rates, when those repair shops will not be repairing the vehicle, results in arbitrary, unsupported and unreasonable settlement amounts.

Section 2695.8(h) **Amend** (Re-lettered)

Current subsection 2695.8(g)(3) is now designated subsection 2695.8(h) as it makes more sense as a separate subsection from subsection 2695.8(g).

Section 2695.8(i) **Amend** (Re-lettered)

Current subsection 2695.8(f) is now designated subsection 2695.8(i) because of other changes made to subsection 2695.8, noted above. The standard for determining repair costs is to base costs upon the prevailing rates in the local market area of the claimant. Language was added to this subsection to formalize this standard. Minor changes were also made for grammatical reasons or for clarity.

Section 2695.8(i)(2) **Amend** (Re-lettered)

Current subsection 2695.8(f)(2) is now designated 2695.8(i)(2). The language of this subsection is revised to clarify that when there is a dispute as to the cost of repairs and the insurer names a repair shop that can make the repairs for the amount of the insurer's written estimate, the insurer shall "cause the damaged vehicle to be restored to its condition prior to the loss at no additional cost to the claimant other than as stated in the policy or as otherwise allowed by these regulations." This added language mirrors the requirement set forth in proposed section 2695.8(f) when an insurer suggests or recommends a repair shop.

Section 2695.8(i)(3) **Amend**

Current subsection 2695.8(f)(3) is now designated subsection 2695.8(i)(3). Language of this subsection is revised to clarify that when there is a dispute as to the cost of repairs and the insurer adjusts the estimate prepared by the shop of claimant's choice, the insurer must provide claimant with a copy of this adjusted estimate.

Section 2695.8(j) (Re-lettered only)

Current subsection 2695.8(g) is now designated subsection 2695.8(j).

Section 2695.8(j)(4) **Amend**

Minor grammatical changes are made to this section.

Section 2695.8(j)(5) **Adopt**

The language in this newly adopted subsection incorporates the requirement of Business and Professions Code Section 9875.1 that insurers disclose to consumers in a written estimate prior to repairs being made that non-original equipment manufacturer replacement crash parts will be used.

Section 2695.8(k) (Re-letter only)

Current subsection 2695.8(h) is re-lettered subsection 2695.8(k)

Section 2695.8(i) **Repeal**

This subsection is repealed and is modified and moved to subsection 2695.7(p) so as to apply to all lines of insurance and

not just auto insurance.

Section 2695.8(j) **Repeal**

This subsection is repealed and is modified and moved to subsection 2695.7(q) so as to apply to all lines of insurance and not just auto insurance.

Section 2695.8(l) **Amend** (Re-lettered)

Current subsection 2695.8(k) is re-lettered subsection 2695.8(l). Language is deleted as it is redundant to newly adopted subsection 2695.7(b)(5).

Section 2695.8(m) **Amend** (Re-lettered)

Current subsection 2695.8(l) is re-lettered subsection 2695.8(m). This section is also amended to clarify the reasonable standard to be used in payment of towing and storage charges. Most automobile insurance policies issued in California place an affirmative duty upon the insured to protect the automobile from further loss. These policies also confer upon the insurer the duty to reimburse the insured for all reasonable fees incurred in protecting the vehicle. When reasonable fees are incurred in towing the vehicle from the scene of the accident and storing the vehicle, these fees should be paid as a matter of course in all auto insurance claims. Although most insurers do reimburse these fees, a trend has developed to limit or exclude reimbursement of these reasonable fees. The Commissioner considers this trend to be against public policy. Language was added to set forth this reasonable standard.

Section 2695.8(m) **Repeal**

Current subsection 2695.8(m) is deleted as it does not contemplate situations where the insured is unable to use the insurer identified tow company due to reasons beyond his or her control such as being unconscious from an accident or non-response from the insurer's tow company.

NOTE: Section 2695.8 **Amend**

California Business and Professions Code Section 9875.1 is added as reference in connection with the added specification in these regulations that insurers disclose the use of non-original equipment manufacturer replacement crash parts.

Section 2695.85. Auto Body Repair Consumer Bill of Rights

Title Adopt

This new section is adopted to implement recently enacted Senate Bill SB1988, which became effective January 1, 2001 and created California Insurance Code Sections 1874.85 and 1874.87. California Insurance Code Section 1874.87 requires the Department to develop an Auto Body Repair Consumer Bill of Rights as a standardized form that insurers are required to provide to their insureds. The Bill of Rights lists certain specific entitlements insureds have concerning the repair of their automobile following a loss.

Section 2695.85(a) Adopt

The language in this adopted subsection describes what actions must be taken by insurers to comply with the requirements of Insurance Code Section 1874.87. Insurers are required to provide a copy of the standardized Bill of Rights at the time of application for automobile insurance or at the time a claim is made. This section also outlines to whom the Bill of Rights must be provided.

Section 2695.85(b) Adopt

The language in this adopted subsection clarifies the types of insurance policies that are subject to the requirements of this subsection. Insurance Code Section 1874.87 applies to all insurers that issue automobile liability or collision policies. As no distinction is made within the statute, this section applies to both commercial and personal automobile policies.

Section 2695.85(c) Adopt

This adopted subsection provides the language for the standardized form developed by the Department as required under Insurance Code 1874.87. The specific language of the form mirrors the requirements set forth in Insurance Code Section 1874.87, Business & Professions Code Sections 9884.8 and 9884.9, and subsection 2695.8(e), (f), (g), and (m) of these regulations.

Note: Section 2695.85 Adopt

The statutes that provide the authority to adopt this subsection are as follows:

Insurance Code Section 790.10 authorizes the Commissioner to enact any regulations necessary to implement and/or administer the Unfair Practices Act (Insurance Code Section 790 *et seq.*)

Insurance Code Section 1874.87 authorizes the Department to develop an Auto Body Repair Consumer Bill of Rights.

The statutes cited as references reflect the sections setting forth the specific entitlements stated in the Bill of Rights:

Insurance Code Sections 790.03(c) and 790.03(h)(3) reflect the unfair claims practices addressed by Insurance Code Section 1874.87.

Insurance Code Section 1874.87 sets forth what specifically must be included in the Bill of Rights.

Business & Professions Code Sections 9884.8 and 9884.9 mandate that automotive repair dealers must provide customers with a written estimate and a detailed invoice. The estimate and invoice must include an itemized bill of parts and labor and identify all parts as new, used, after market, reconditioned, or rebuilt.

Section 2695.9. Additional Standards Applicable to Fire and Extended Coverage Type Policies with Replacement Cost Coverage.

Title **Amend**

The title of existing section 2695.9 is changed to clarify that the section applies to all types of first party residential and commercial property insurance claims, not just replacement cost policies.

Section 2695.9(a) **Adopt**

The language in this newly adopted subsection reflects current case law. The cost of repair or replacement of a building or any part of it includes any cost the insured is reasonably likely to incur in repairing or replacing the covered loss such as a general contractor's overhead and profit.

Section 2695.9(b) **Amend** (Re-letter)

This subsection was re-lettered to subsection 2695.9(b) from previous subsection 2695.9(a) due to the proposed adoption of subsections 2695.9(a). The language was also revised to clarify that the subsection applies to all types of first party residential and commercial property insurance claims not just replacement cost policies.

Section 2695.9(c) **Adopt**

The language in this newly adopted subsection was added for consistency, to mirror standards set forth in subsection 2695.8(e) for automobile claims.

Section 2695.9(d) **Adopt**

The language in this newly adopted subsection was added for consistency and to approximate standards set forth in subsection 2695.8(f) for automobile claims.

Section 2695.9(e) **Adopt**

The language in this newly adopted subsection was added for consistency and to approximate standards set forth in subsection 2695.8(i) for automobile claims.

Section 2695.9(f) **Adopt**

The language in this newly adopted subsection was added to address the problem of delay in appraisals caused by insurers that request discovery, subpoenas of evidence, expert testimony and other tools associated with civil litigation. The raising of outside issues causes the appraisal process to become a prolonged, cost prohibitive, trial rather than an economical, swift alternative for determining covered damages.

NOTE-Section 2695.9 **Amend**

Business and Professions Code Section 7109, which relates to proper construction standards that contractors must follow when repairing homes, was added as authority.

Section 2695.10. Standards Applicable to Surety Insurance.

Section 2695.10(a) **Delete**

This subsection is deleted as similar language already exists at subsection 2695.7(a). Certain minimum standards set forth in the regulations should and do apply to claims brought under surety bonds. Section 2695.7 of the regulations does not impede the surety's ability to conduct its business efficiently and fairly and in accordance with California Insurance Code Section 790.03(h).

Section 2695.10(b) **Delete**

This subsection is deleted as similar language already exists at subsection 2695.7(b). There is no legitimate reason to give surety insurers up to 60 days to accept or deny a claim and all other insurers only up to 40 days. Certain minimum standards set forth in the regulations should and do apply to claims brought under surety bonds. Subsection 2695.7(b) of the regulations does not impede the surety's ability to conduct its business efficiently and fairly and in accordance with California Insurance Code Section 790.03(h).

Section 2695.10(c) **Delete**

This subsection is deleted as similar language already exists at subsection 2695.7(c). Certain minimum standards set forth in the regulations should and do apply to claims brought under surety bonds. Section 2695.7 of the regulations does not impede the surety's ability to conduct its business efficiently and fairly and in accordance with California Insurance Code Section 790.03(h).

Section 2695.10(d) **Delete**

This subsection is deleted as similar language already exists at subsection 2695.7(d). Certain minimum standards set forth in the regulations should and do apply to claims brought under surety bonds. Section 2695.7 of the regulations does not impede the surety's ability to conduct its business efficiently and fairly and in accordance with California Insurance Code Section 790.03(h).

Section 2695.10(e) **Delete**

This subsection is deleted as similar language already exists at subsection 2695.7(l). Certain minimum standards set forth in the regulations should and do apply to claims brought under surety bonds. Section 2695.7 of the regulations does not impede the surety's ability to conduct its business efficiently and fairly and in accordance with California Insurance Code Section 790.03(h).

Section 2695.10(f) **Delete**

This subsection is deleted as similar language already exists at subsection 2695.7(h). There is no legitimate reason to give surety insurers only 15 days to pay claim and all other insurers up to 30 days. Certain minimum standards set forth in the regulations should and do apply to claims brought under surety bonds. Subsection 2695.7(h) of the regulations does not impede

the surety's ability to conduct its business efficiently and fairly and in accordance with California Insurance Code Section 790.03(h).

Section 2695.10(g) **Delete**

This section is deleted as the language is adequately covered in subsection 2695.7 which subsection is applicable to surety insurers, and in the proposed adopted language set forth below.

Section 2695.10(a) **Adopt**

This newly adopted subsection specifies additional claim standards that are applicable to surety insurers but that are not in subsection 2695.7.

Section 2695.10(b) **Adopt**

This newly adopted subsection specifies additional claim standards that are applicable to surety insurers but that are not in subsection 2695.7.

Section 2695.10(c) **Adopt**

This newly adopted subsection specifies additional claim standards that are applicable to surety insurers but that are not in subsection 2695.7.

NOTE-Section 2695.10 **Amend**

Deletions are made from authority and reference that coincide with the deletions to the 2695.10 subsections.

Section 2695.11. Additional Standards Applicable to Life and Disability Insurance Claims.

Section 2695.11(a) **Amend**

The current language of this regulation protects certain insureds by setting minimum criteria that must be adhered to before an insurer can seek an offset of future claims based upon an overpayment of a prior claim. However, the current language ignores those insureds who do not have future claims to offset (that is, in cases where the insured has no future claims to offset, the insurer can seek reimbursement of an overpayment without adhering to the requirements set forth in subsection 2695.11(a)(1) or (2). By adding "seek reimbursement of an overpayment" and deleting "on a prior claim arising" to

subsection 2695.11(a) and adding "the reimbursement or" to subsection 2695.11(a)(1), insureds who have future claims and those who do not are afforded the same protections.

Section 2695.11(a)(1) **Amend**

In order to be consistent with the change to subsection 2695.11(a), this subsection is amended to add the words "the reimbursement or" are added. In addition, the word "such" is deleted and replaced with "the" for grammatical reasons.

Section 2695.11(d) **Adopt**

The language in this newly adopted subsection was added in response to complaints from the California Medical Association and other sources. The time frames specified in subsection 2695.7 were mistakenly made inapplicable to disability claims presumably because Insurance Code Section 10123.13 specifies the time period within which a disability claim must be accepted or denied. However, a mechanism is needed to prompt an insurer to make a decision (i.e., accept or deny) regarding a contested claim) within a reasonable time and to provide the claimant and assignee written notice of the need and reasons for additional time to make such a decision.

Section 2695.11(e) **Adopt**

The language in this newly adopted subsection is added to require an insurer or its representative to give timely pre-authorizations of non-emergency services. The scope of the pre-authorization must be explained in writing and must specify that the pre-authorization is not a guarantee that the non-emergency surgery is a covered expense under the policy or that the claim will be paid.

Section 2695.11(f) **Adopt**

The language in this new subsection is added in response to consumer complaints to clarify that an insurer may not require a pre-authorization in an emergency.

Section 2695.11(g) **Adopt**

The language in this newly added subsection is added to clarify that insurers that request copies of medical records must, as part of their claims investigation costs, reimburse the insured or medical service provider for the cost of copying those medical records.

Section 2695.11-NOTE **Amend**

Insurance Code Section 10123.13, which addresses the time for reimbursement of uncontested claims and which also defines "contested claim", was added as reference.

Section 2695.12. Noncompliance and Penalties.

Section 2695.12 Title **Amend**

The title of existing section 2695.12 is changed to clarify that the section applies only to the penalties to be assessed for violations of the regulations.

Section 2695.12(a) **Repeal**

As the word "knowingly" is now defined in subsection 2695.2(1) this subsection has been repealed as the language is unnecessary, confusing, and not applicable to the 2695.12 Penalties section.

Section 2695.12(b) **Amend** (Re-letter)

This subsection is re-lettered to Section 2695.12(a) as current Section 2695.12(a) is repealed, as noted above. This subsection has also been amended to reflect that the factors described in this subsection go to the appropriate penalties to be assessed and not to whether a violation of any of the sections of the regulations has occurred.

Section 2695.12(a)(2) **Amend** (Re-letter)

The word "California" is added before the words "Insurance Code" for clarification purposes.

Section 2695.12(a)(7) **Amend** (Re-letter)

The words "noncomplying act(s)" have been replaced with "violations" to clarify that noncomplying acts are violations of the regulations. Additional language changes were made because, in order to determine the appropriate penalties to be assessed, the Department must consider the number of claims where violations have been found as contrasted to the number of claims examined by the Department. The current ratio using the number of claims handled by the insurer is not relevant in determining appropriate penalties as the Department does not examine all claims handled by insurers and would have no way of knowing whether violations would be found in those claim files not reviewed.

Section 2695.12(a)(8) **Amend** (Re-letter)

The words "noncomplying act(s)" have been replaced with "violation(s)" for the same reason as noted above.

Section 2695.12(a)(10) **Amend** (Re-letter)

The word "noncompliance" has been replaced with "violation" for the same reason as noted above.

Section 2695.12(a)(11) **Amend** (Re-letter)

A punctuation change was made for grammatical purposes.

Section 2695.12(a)(12) **Amend** (Re-letter)

Minor punctuation and other changes were made for grammatical purposes.

Section 2695.12(a)(13) **Adopt**

This newly adopted subsection contains similar language moved from subsection 2695.12(a)(3)(B), which is repealed. Minor grammatical changes were also made.

Section 2695.12(c) **Repeal**

This subsection is repealed as it is ambiguous and its intent is encompassed in the language of subsection 2695.12(a)(11).

Section 2695.13. Severability.

No changes.

Section 2695.14. Effective Dates.

Section 2695.14(a) **Amend**

Modifications were made to this subsection for reasons of clarity.

Section 2695.14(b) **Amend**

Modifications were made to this subsection for reasons of clarity.

Section 2695.14(c) **Amend**

Modifications were made to this subsection for reasons of clarity.

NOTE: Section 2695.14 **Amend**

Minor non-substantive changes were made to the Authority for this subsection for clarification purposes.

IDENTIFICATION OF STUDIES:

There are no specific studies relied upon in the adoption of this subchapter.

SPECIFIC TECHNOLOGIES OR EQUIPMENT:

Adoption of these regulations would not mandate the use of specific technologies or equipment.

ALTERNATIVES:

The Commissioner has determined that no reasonable alternative exists to carry out the purpose for which the regulations are proposed. Performance standards were considered but were rejected as an unreasonable and impracticable alternative in the context of regulations that seek efficiently to define specific procedures that constitute fair business practices in the settlement of insurance claims.

ECONOMIC IMPACT ON SMALL BUSINESS:

The Commissioner has identified no reasonable alternatives to the presently proposed regulations, nor have any such alternatives otherwise been identified and brought to the attention of the Department, that would lessen any impact on small business. Although performance standards were considered as an alternative, they were rejected, in part, because they would increase, rather than lessen, the impact upon small business. Unlike the proposed regulations, performance standards would not provide small businesses an efficient means of knowing how to comply, or of ensuring they have achieved compliance. Further, it could be necessary that small businesses incur the additional expense of legal fees charged by lawyers whose services might be required in order to interpret a performance standard. Finally, because of this indefiniteness, performance standards would be likely to breed costly litigation, which small businesses in particular can ill afford.

PRE-NOTICE DISCUSSIONS:

Pursuant to Government Code Section 11346.45(a), public discussions were held on December 18 and 19, 2001 regarding proposed amendments to these regulations. Interested and affected parties were given an opportunity to present statements or comments with respect to the proposed amendments. The Commissioner considered these statements and comments and some changes were made to the proposed amendments in response.